Quantity
Pre-Assessment Survey

Internal Control Technical Guide

NOTE: An extensive review of internal control for quantity should be conducted when some specific risk exists related to quantity. For example, when specific or compound duty rates are based on quantity then quantity may represent a risk that should be addressed. Quantity may be a risk area for imports of petroleum, footwear, alcoholic beverages, watches, commodities subject to quota and others. If the audit discloses significant unacceptable practices related to quantity, such as routinely declaring numbers of containers rather than number of units, these unacceptable practices should be addressed by the PAS team working with the company in the most efficient, effective manner.

Objective

Provide guidance in performing a Pre-Assessment Survey (PAS) of the company's internal control for Quantity and evaluating the results.

Background

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this technical guide are based on *Assessing Internal Controls in Performance Audits,* GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and American Institute of Certified Public Accountant's *Statement on Auditing Standards No. 78.*

Title 19 U.S.C. 1484(f) states that all import entries shall include an accurate statement specifying the quantities of all merchandise imported and the value of the total quantity of each kind of article. This is also required in General Statistical Note 1(a)(xii) to the HTSUS, 19 CFR 141.61(e), and Customs Directive 099-3550-061 (Instructions for Preparation of the CF 7501).

Title 19 CFR 141.86(a)(4) states that each invoice of imported merchandise shall set forth the quantities in the weights and measures of the country or place from which the merchandise is shipped, or in the weights and measures of the United States.

Title 19 CFR 142.6(a)(2) requires the commercial invoice or other acceptable documentation contain the quantities of the merchandise.

Examples of Red Flags

The following examples are conditions that may indicate a potential problem with Quantity.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring correct quantity for Customs purposes. Examples:
  - ✓ Company does not monitor or interact with the broker on quantity issues.

  - ✓ Company relies on one employee to handle quantity issues, and there are poor or no management checks or balances over this employee.
- Company import staff lacks knowledge of quantity issues.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- Significant variance exists between the importer's data and Customs data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with quantity (e.g., steel kilogram vs. tonnage issue).
- Company imports merchandise subject to restrictions including specific or compound duty rates, admissibility issues, or quota/visa.
- Quantities reported on the invoice, entry, packing slip, and receiving report do not match.
- The company has no receiving reports or documentation of quantities received (parts shipped to Quality Assurance Dept. and not counted).
- Quantity documents report different units of measure than required by Customs (lbs. vs. kg. , carton vs. cases).
- Company has numerous drop shipments for which quantities cannot be verified (shipment directly to the customer).
- The receiving department has authority to override quantity variances between actual receipt and the packing list or other shipping documents.
- The company uses overseas vendor count for quantities received.
- Special handling requirements prohibit accurate count (e.g. silicon wafers require "clean area").
- Merchandise changes quantity because of expansion/contraction of commodities (e.g. petroleum, resins/polymers).

Examples of Best Practices

- Internal controls over Quantity:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the import department, including correct imported quantity. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- Internal control procedures assign quantity verification duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about quantity matters.
- Company conducts and documents periodic reviews of quantity, and uses the results to make corrections to entries and changes to their import operations as appropriate.
- Company has appropriate controls in place to monitor quantities of merchandise entered under specific or compound duty rates, quota/visa, or other admissibility issues.
- Company has a system to verify quantities reported on the invoice, entry, packing slip, and receiving report, and generates a discrepancy report.
- Quantity discrepancies are recorded in a log and reported to Customs.
- Company has table of conversions for units of measure as required by Customs.
- Override of quantity variances by the receiving department requires authorization by appropriate personnel.

- Company reviews overseas vendor count for quantities received.
- Company uses industry standards for expansion/contraction of commodities (e.g. petroleum, resins/polymers).

Examples of Documents and Information to Review

- Internal control policies and procedures for ensuring proper reporting of quantities entered under specific or compound duty rates, quota/visa, or other admissibility issues.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to quantity.
- Company's documentation that supports monitoring and verification of established and/or written internal control for quantity such as:
  - ✓ CF 7501 Entry Summary document.
  - ✓ CF 214 if applicable.
  - ✓ Commercial invoice with additional information affecting admissibility.
  - ✓ Bill of lading, packing slip, in-bond documents, and receiving reports.
  - ✓ Purchase Order, contracts or agreements.
  - ✓ Quantity discrepancy reports.
  - ✓ Gauge Report for commodities (e.g. petroleum, resins/polymers).

Suggested Testing

PAS team judgement should be used to determine the type and amount of testing needed to evaluate how effective internal control is and to determine if there is sufficient risk to warrant proceeding to Assessment Compliance Testing (ACT.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. The **risk exposure**, and

2. The **internal control** system, by determining if the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

Risk Exposure

Risk exposure is the probability of significant Customs noncompliance. In each step of determining risk exposure, consideration should be given to:

1. Significance [to Customs] and sensitivity [e.g., issues of interest to congress or the media, or impacting admissibility].

2. Susceptibility [of making incorrect declarations].

3. The existence of any "red flags."

4. Management support [of strong internal control].

5. Competent personnel [to adequately administer the controls].

Steps to Determine Risk Exposure:

1. Evaluate problems identified in the profile, compliance measurement rates, questionnaire, and concerns raised by the import specialist and account manager.

2. Perform the macro risk analysis tests.

3. Analyze the macro risk analysis tests results to determine the risk exposure level.

4. Evaluation of risk exposure is not simply a one-time process that occurs at the start of the PAS process. Continually reassess risk exposure as more information is gathered from evaluating internal control and performing other work in the PAS.

Macro Risk Analysis Examples

Example A: Low Risk Exposure

The profile identified Customs entries with compound duty rates. The team discussed the issue with the company in order to identify the products that are related to the compound duty rate issues. CAS obtained a database of products with compound duty rates. It was determined that the total quantity identified in this database closely approximated the amounts reported in Customs ACS records. Using “walk through” entries, the team compared Customs reported quantities subject to compound duty rates to the company’s quantities listed on the invoices and receiving reports and found no discrepancies. The team considered this to be low risk.

Example B: High Risk Exposure

Validation of company control activity research indicated that the importer had previously submitted a quota entry where the visa did not match the commercial invoice or packing list. No corrected entry was submitted to Customs. This issue was discussed with the company in order to determine the adequacy of internal control in place to prevent this type of problem from occurring and the cause and extent of this problem. The CAS obtained a database of all products subject to quota. It was determined that the total quantity identified in this database did not approximate the quota amounts reported to Customs. The team considered this to be high risk.

System of Internal Control

To evaluate the internal control system:

1. Consider the five components of internal control:

    - Control Environment.
    - Risk Assessment.
    - Control Activities.
    - Information and Communication.
    - Monitoring.

2. Review relevant Customs and company documents to identify and understand relevant internal control over quantity. (Examples of documents and information to review are listed on prior pages.)

3. Determine whether the company established and follows procedures. Review:

   - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
   - Documentary evidence (such as a log) of communication with the broker and company departments on quantity issues. This includes company testing of broker operations and verification that the broker followed company instructions.
   - Documentary evidence of inter-company communications to ensure correct quantity information is provided to Customs.
   - Training records and materials relating to quantity are used to educate staff on Customs matters.

4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the "Worksheet for Evaluating Internal Control over Quantity".

   Note: The internal control assessment should include Steps to:

   - Identify and understand internal control.
   - Determine what is already known about control effectiveness.
   - Assess the adequacy of internal control design.
   - Determine whether controls are implemented and effective.
   - Determine whether transaction processes are documented.

Extensiveness of Audit Tests (Testing Limit)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, test the appropriate number of controls and associated transactions using the table below.

Determine Extensiveness of Audit Tests

Risk Exposure	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15

Risk Exposure	+	Preliminary Review Internal Control	=	Extensiveness of Audit Test	Testing Limit
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits.*
Column titled "Testing Limit" reflects Customs test sizes.

Evaluation of Pre-Assessment Survey Testing Results

The following steps are guidance for determining the effectiveness of company's internal control over reporting correct quantity.

1. Complete the "Worksheet for Evaluating Internal Control Over Quantity" to determine whether risk determination is acceptable or unacceptable and document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

   Customs considers risk unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining if conditions warrant proceeding to ACT.

   - **Do not proceed to ACT (Revenue) if:**
     - ✓ Cost-benefit analysis warrants no further effort (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant).
     - ✓ The PAS indicated that the quantity error was due to an isolated incident.
     - ✓ The company agrees with PAS finding(s) and agrees to quantify the quantity errors within an acceptable timeframe.

   - **Do not proceed to ACT (Compliance) if:**
     - ✓ The error was isolated, and the importer can show identical entry lines with value correctly reported.
     - ✓ The quantity errors were systemic, and the importer agrees to develop and implement a compliance improvement plan within an acceptable time frame.

   - **Proceed to ACT (Revenue) if:**
     - ✓ The company does not have adequate internal control, and PAS indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
     - ✓ Importer will not quantify loss of revenue.

   - **Proceed to ACT (Compliance) if:**
     - ✓ The company refuses to take corrective action on systemic errors, and it is necessary to calculate a compliance rate.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

Examples

The following examples of situations that might be encountered under PAS *are for clarification purposes only*.

Example A: Situation in which the team would not proceed to ACT (Revenue)

Company A imports textiles subject to quota/visa requirements from a related party located in Hong Kong. The company did not have written internal control procedures for quantity. The receiving department was not aware of any Customs requirements to report quantity variances to the Import department. The company relied on the quantity stated on the invoice/packing list from overseas vendors and did not perform a physical count. A review of the receiving records revealed that the importer received more than the quantity declared to Customs. This discrepancy resulted in a loss of duty. ACS data showed only two previous entries from this vendor with an insignificant value amount. During the review, the company paid the duty and established written internal control procedures to verify quantity received. The PAS team was able to verify that the procedures were effective, therefore, there was no need to proceed to ACT.

Example B: Situation in which the team would not proceed to ACT (Compliance)

Same as Situation A, except that after further review, it was determined that the errors were systemic but the importer agreed to develop and implement a compliance improvement plan within two months. Therefore, there was no need to proceed to ACT.

Example C: Situation in which the team would proceed to ACT (Revenue)

Company C imports steel from Lithuania. Steel is sold in tons. The tonnage must be converted to kilograms (kilos) in order to make entry, since duty is assessed on kilos instead of tons. The conversion from tons to kilos made by the company was not verified for accuracy. The conversions were not followed as prescribed in their operations handbook. This resulted in a major understatement of weight for the steel and the proper duty was not paid. After further review, we found problems with the methodology of the formula calculation for conversions. Since the company was unwilling to quantify loss of revenue, the team proceeded to ACT

Example D: Situation in which the team would *proceed to ACT (Compliance)*

Same as Situation C except that the company refused to establish internal control procedures to ensure that the correct quantity is reported to Customs. Therefore, the team proceeds to the ACT process.

Worksheet for Evaluating Internal Control Over Quantity

Objective: Determine whether the company has procedures designed to effectively control Customs risks related to quantity.

Risk Determination:

Acceptable _____
Unacceptable _____

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Are internal controls over quantity formally documented?						
Are written policies and procedures for quantity for specific or compound duty rates, quota/visa, or other admissibility issues approved by management?						
Are written policies and procedures reviewed and updated periodically?						
Do written internal control procedures assign responsibility for quantity to a position rather than an individual?						
Does the company have good interdepartmental communication concerning quantity issues?						
Is only one department/individual primarily responsible for assuring compliance with quantity requirements?						

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Does the individual overseeing quantity compliance have adequate knowledge and training and the authority to ensure that internal control procedures for quantity are established and followed by all company departments?						
Are internal controls over quantity periodically tested?						
Were the results of the periodic internal control tests documented?						
If weaknesses were found during internal control testing, were corrective actions implemented?						
Does the company use conversions for units of measure as required by Customs?						
Is the quantity variance override authority limited to appropriate personnel?						
Does the company count quantities received and make a record of such counts and discrepancies?						
Are receiving reports retained and readily available?						
Are receiving reports readily traceable to entry summaries?						

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Is broker notified of quantity variances in order to amend Customs entry summary information?						
Does the company have internal control procedures to address specific issues identified in the profile?						
Does the company have written procedures to take corrective actions as necessary?						
Internal Control Conclusions						
Does company provide adequate broker oversight?						
Did PAS testing verify that control procedures were being followed?						
Did interviews with responsible personnel support control procedures?						
Does the company have internal control to address specific issues identified in the profile?						
List company-specific procedures and controls below (if applicable)						